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## CONTENTS

	Page
Secretary Mellon's Defense of U. S. Debt Funding Policy .....	138
Reply of the British Chancellor of the Exchequer .....	138
Statement of the American Treasury Department .....	139
British Expenditures in the United States .....	139
Mr. Churchill's Interpretation .....	140
American Explanation of Credit Items .....	141
Loans for "Commercial" as distinguished from "War Purposes" .....	141
Divergent Interpretations of Britain and United States .....	142
Britain's Contention re Borrowing in Behalf of Allies .....	142
American Explanation of British Borrowings .....	143
Evidence of Secretary Mellon .....	143
Alleged "Discrimination" Against Great Britain .....	145
Larger Aspects of the Debt Controversy .....	146

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## The British-American Debt Controversy

THE storm of controversy that broke on both sides of the Atlantic upon the publication of Secretary Mellon's recent letter to Mr. Frederick W. Peabody, in which the Secretary of the Treasury made a vigorous defense of the debt funding policy of the United States, has raised several important questions of fact and interpretation which bear directly upon the debt funding policy of the United States. Mr. Winston Churchill, British Chancellor of the Exchequer, took the occasion of the debate on the Anglo-French debt to contradict sharply statements made by the American Secretary, and declared that Mr. Mellon had been "either misreported or misled." Under-Secretary Winston of the American Treasury replied to Mr. Churchill by issuing a Treasury statement of the British account with the United States, and the British Chancellor responded with a lengthy statement from the British Treasury.

The dispute between Mr. Mellon and Mr. Churchill has had its reverberations throughout Europe and especially in France where

the Mellon-Berenger agreement is pending ratification by the French Parliament. Emerging from a long period of obscure retirement Georges Clemenceau, the war premier of France, addressed an open letter to President Coolidge on August 8 in which he appealed to the President not to consider the French debt as a purely commercial proposition but to take into account the present financial difficulties in France and her great sacrifices during the war. The war premier also warned President Coolidge that "France is not for sale" and criticized the attitude of the United States toward the former allies by comparing the separate peace made by the United States with that negotiated by Russia at Brest-Litovsk. No reply has yet been made to M. Clemenceau with the exception of the announcement that the President considered the debt agreement as closed.

Aside from the unusual and spectacular features of a running debate between the Treasury departments of Great Britain and the United States, are the important questions of fact and implications of policy in-

volved in the controversy. What were the amounts of British expenditures in the United States? What proportion of the British debt was accumulated for purely commercial as distinguished from war purposes? To what extent was the British debt incurred in behalf of the other Allies? Was Great Britain unjustly discriminated against in the debt funding agreements with the United States? What commitments for the cancellation of the debts were made by the United States at the time they were incurred? These are the outstanding questions involved in the recent controversy.

#### **SECRETARY MELLON'S LETTER**

Secretary Mellon's letter was written in reply to an impassioned plea sent by Mr. Peabody to President Coolidge on June 30, advocating cancellation of all war debts owed to the United States by the Allied nations. Secretary Mellon's letter may be briefly summarized as follows: 1. That when the advances to the Allied governments were made "they knew and we knew that they were loans, not gifts . . . The only question for discussion in each settlement has been the extent of the capacity of the debtor to make payments on the acknowledged liability." 2. The allies to which we made advances while the war was on are England, France, Italy, Belgium, Serbia and Russia, and therefore the loans to these nations are the only ones which can be considered as entering into the controversy. In the case of Finland, Esthonia, Latvia, Lithuania, Poland, Czechoslovakia, Hungary, Austria, Armenia and Roumania, the loans were not made until after the Armistice was signed, and are therefore of a purely commercial nature. 3. The relation of the burden of our debt settlements with the allied governments to our loans after the Armistice is summarized by Secretary Mellon as follows: In the case of England, post armistice advances with interest amounted to \$660,000,000 and the present value of the entire debt settlement is \$3,297,000,000. France's post armistice indebtedness with interest amounts to \$1,655,000,000. The present value of the pending debt funding agreement with France is \$1,681,000,000.

The post armistice borrowings of Belgium were \$258,000,000 and the present value of the settlement is \$192,000,000. The post armistice borrowings of Italy with interest are \$800,000,000 and the present value of its debt is \$426,000,000.

The part of Secretary Mellon's letter which provoked the reply from the British Chancellor of the Exchequer referred to the expenditure of the money borrowed by England from the United States. Secretary Mellon said: "It must be remembered that England borrowed a large proportion of its debt to us for purely commercial as distinguished from war purposes . . . to meet its commercial obligations maturing in America, to furnish India with silver, to buy food to be resold to its civilian population, and to maintain exchange. Our loans to England were not so much to provide war supplies as to furnish sterling for home and foreign needs and to save England from borrowing from its own people."

#### **MR. CHURCHILL'S REPLY**

The response to Mr. Mellon's letter in England was almost immediate. Mr. Hilton Young, former Liberal financial Secretary of the Treasury, and now a member of the Conservative party, and Mr. Philip Snowden, former Labor Chancellor of the Exchequer, in the debate on the Anglo-French debt settlement, took advantage of the occasion to attack the debt-funding policy of the United States. Mr. Winston Churchill, speaking from the ministerial bench, after quoting the paragraph of the Mellon letter in which the American Secretary said that a large proportion of the English borrowings from the United States were "for purely commercial as distinguished from war purposes" declared, "There really is a complete misapprehension of the facts of the case and so serious is this misapprehension that it makes me almost doubt the authenticity of the passage which I quote." Mr. Churchill asserted that England, like all the other Allies, had spent vast sums of money in the United States for food as well as for munitions, but that all the loans were by Act of Congress specifically limited to the purpose of prosecuting the war. With reference to the British expenditure of money

in the United States Mr. Churchill's statement is as follows:

"Between 1917 and the end of the war,—that is during the period of America's intervention,—we spent over \$7,000,000,000 in the United States, and of that sum borrowed \$4,000,000,000, and we provided \$3,000,000,000 additional, spent in the United States, from our own and other resources. Against the \$4,000,000,000 that we borrowed, we spent over \$1,500,000,000 on munitions and over \$2,500,000,000 on cereals and other essential foodstuffs, so that on these two heads alone we spent a sum which equals the whole sum that we borrowed from the United States.

"As to the special instances cited by the distinguished foreign statesman whose name I have mentioned, there again it seems he has either been misreported or misled. We spent on commercial maturities during this same period \$354,000,000 out of a total of \$7,200,000,000 which we borrowed or provided from our own resources or rather less than one-twentieth of the total dollar expenditure for which we were responsible."

#### UNDER-SECRETARY WINSTON'S STATEMENT

In reply to Mr. Churchill's statement that Great Britain had provided \$3,000,000,000 from its own resources, Under-Secretary Winston of the American Treasury, on July 20, issued the following statement of the British account with the United States:

Munitions, including remounts ..	\$1,330,607,883.09
Munitions for other Governments	205,496,801.10
Exchange and cotton purchases .	1,682,419,875.31
Cereals .....	1,375,379,343.57
Other foods .....	1,169,153,585.05
Tobacco .....	99,174,858.34
Other supplies .....	215,331,787.01
Shipping .....	48,890,000.00
Reimbursements .....	19,302,367.55
Interest .....	387,732,633.50
Maturities .....	353,501,561.66
Relief .....	16,000,000.00
Silver .....	261,643,388.81
Food for Northern Russia .....	7,029,965.94
Miscellaneous .....	47,745,029.01

Total reported expenditures ..\$7,219,408,669.94

These expenditures were met as follows:

By reimbursement from the other Allies out of funds loaned to these Allies by the United States .....	\$1,853,612,246.37
By dollar payments by the United States Government for British currencies .....	449,496,227.55
By proceeds of rupee credits and gold from India .....	81,352,908.06
By cash from Britains "own inde- pendent resources" .....	760,128,929.52
Funded in debt settlement with the United States .....	4,074,818,358.44

Total .....\$7,219,408,669.94

According to Mr. Winston's statement, only \$760,000,000 were paid out of Britain's "own independent resources." \$1,853,000,000 were provided by the other Allies out of loans negotiated from the United States, and Great Britain acted merely as the purchasing agent for the other governments in this transaction.

#### MR. CHURCHILL'S REJOINDER

In reply to the statement of the American Treasury, the Chancellor of the Exchequer, on July 22, issued a lengthy statement in which he "notes with approval" that there is no disagreement on the fact that out of a total of \$7,219,000,000 spent by Great Britain in the United States from 1917 to 1919, only \$4,074,000,000 were borrowed money. In reviewing the items in detail Mr. Churchill took issue with the American Treasury on the assertion that the \$1,682,000,000 spent by Great Britain on exchange was not necessary for purchases in America, but enabled Britain to make purchases in other countries at undepreciated exchange rates. After quoting the official United States Treasury Report for 1920 that the "exchange item" reflects purchases of wheat, food, cotton, leather and oil, Mr. Churchill further declared that the post-armistice loans to Great Britain of \$581,000,000 were used largely to pay for American goods the contracts for which had been made previous to the signing of the Armistice.

#### BRITISH EXPENDITURES IN THE UNITED STATES

The first point raised by Mr. Churchill in refuting Mr. Mellon's argument is concerned with the expenditures of the British

government in the United States for the period from April, 1917 to November, 1920. In spite of this apparent disagreement there is, in reality, little dispute as to the fact of how the money was spent. The real points at issue depend upon what interpretation is given to the various items in the expenditure and loan accounts of

the two governments. The following table compiled from official sources by Mr. Harvey E. Fisk and presented in "The Inter-Ally Debts" shows the advances made by the United States to the British government and the total expenditures reported by Great Britain for the period from April, 1917 to November 1, 1920:

**ADVANCES MADE BY THE UNITED STATES GOVERNMENT AND EXPENDITURES REPORTED BY GREAT BRITAIN FOR THE PERIODS GIVEN BELOW**  
(In "Currency" dollars — 00,000 omitted)

	Total April 1917 to Nov. 1920	1917 April 6 to Dec. 31	1918 Jan. 1 to June 30	1918 July 1 to Nov. 30	1918-19 Dec. 1 to June 30	1919-20 July 1 to Nov. 1
Advanced .....	4,277,0	1,860,0	1,215,0	721,0	481,0	.....
Refunded .....	80,2	.....	.....	.....	.....	80,2
Net Advanced .....	4,196,8	1,860,0	1,215,0	721,0	481,0	†80,2
Expenditures:						
Munitions .....	1,330,6	570,0	292,1	317,4	151,1	.....
Munitions (for other Governments) .....	205,5	194,8	8,3	9	1,5	.....
Exchange and Cotton .....	1,682,4	1,274,6	272,7	23,4	111,6	.....
Cereals .....	1,375,4	361,9	385,5	467,1	160,8	.....
Other Foods .....	1,169,2	154,6	404,8	319,0	290,7	.....
Tobacco .....	99,2	.....	7,4	56,2	35,6	.....
Other Supplies .....	215,3	21,2	60,7	83,7	49,8	.....
Shipping .....	48,9	48,7	1	1	.....	.....
Reimbursements .....	19,3	.....	.....	.....	.....	19,3
Interest .....	387,7	80,1	75,9	114,0	115,5	2,2
Maturities .....	353,5	15,9	91,9	199,1	46,5	.....
Relief .....	16,0	.....	.....	.....	12,3	3,7
Silver .....	261,6	.....	60,7	72,1	128,8	.....
Food—Northern Russia .....	7,0	.....	.....	7,0	.....	.....
Miscellaneous .....	47,8	4,9	5,2	19,2	18,4	.....
Total Reported Expenditures ..	7,219,4	2,726,8	1,665,4	1,679,3	1,122,8	25,2
Less Reimbursements from United States—Credits to other Governments .....	1,853,6	513,1	295,0	656,3	359,0	30,2
Dollar Payments by United States for foreign currencies .....	449,5	.....	46,3	76,4	158,8	168,1
Proceeds of rupee credits and gold from India .....	81,4	3,4	30,5	33,9	13,6	.....
† Net Expenditures .....	4,834,9	2,210,3	1,293,6	912,7	591,4	* 173,1

The actual figures quoted by Mr. Churchill and Mr. Winston are in substantial agreement and they check roughly with those in the table reprinted above. The only point at issue appears to be one of interpretation. According to Mr. Churchill's statement of the case, the figures should be tabulated somewhat as follows:

Total gross expenditures of

Great Britain ..... \$7,219,408,669.00  
Paid out of Great Britain's own resources consisting of (1) reimbursements from the other Allies; (2) dollars received from the United States in payments for British currencies; (3) proceeds of rupee credits and gold from India; (4) cash; 3,022,500,000.00  
Balance funded in debt settlement with the United States \$4,074,818,000.00

† Repayments in excess of cash advanced.

\* Receipts in excess of expenditures.

‡ On account of five ciphers omitted last digits do not exactly add.



### CREDIT ITEMS IN THE BRITISH ACCOUNT

It is apparent that the issue between the American Treasury and Mr. Churchill depends upon how the three credit items in the British account are classified. These items and an explanation of their meaning follow:

1. "Reimbursements from United States credits to other governments." This item amounts to \$1,853,000,000 and represents goods, chiefly cereals purchased by Great Britain in behalf of the other Allies. In order to reimburse England for these purchases, the allied governments borrowed from the United States, and the sums thus loaned were transferred to the credit of Great Britain's account with the American government. The net effect of these transactions was to reduce the amount of the British indebtedness and increase the indebtedness of the other Allies.

2. "Dollar payments by the United States for foreign currencies." This item amounts to \$449,000,000. It represents American purchases of British currencies with which to pay the expenses of the United States army in England. The United States bought British currency and paid for it by making a bookkeeping entry to the credit of the British government.

Mr. Albert Rathbone, former Assistant Secretary of the Treasury in charge of war purchases describes these transactions as follows:

"For its own war purposes in Great Britain, France and Italy, the United States did not borrow pounds or francs or lire. Our Treasury was obliged to procure these currencies for the use of our army abroad. We bought pounds, francs and lire from the governments of Great Britain, France and Italy, and made payment therefor in dollars here. The dollars thus obtained by Great Britain, France and Italy were applied by them towards the cost of their war purchases here, and thus the amount of the dollar loans required by these countries from our Treasury was diminished in a corresponding sum."

The amount of these purchases of foreign currencies made by the United States in its own behalf is shown in the following table:

	National Currency	Equivalent
France—Francs .	5,711,941,418	\$1,925,438,236
Great Britain—		
Pounds . . . . .	100,572,388	449,496,277

Italy—Lire . . . . .	97,583,743	14,425,092
Belgium—Francs	12,500,000	1,197,556

\$2,490,557,111

3. "Proceeds of rupee credits and gold from India." This item involves a total amount of \$81,400,000 and it is made up from the sale of \$71,000,000 worth of rupee credits to the Federal Reserve Board and \$10,000,000 worth of gold shipped to the United States from India. The British government was given credit for these items against the silver shipments amounting to \$261,600,000 which were transferred from the United States to India.

If the above items can be called payments from the "independent resources" of the British government Mr. Churchill is right in his contention that Great Britain spent about \$3,022,000,000 out of its own resources. If the classification followed by the American Treasury is correct, however, Great Britain's net expenditures after deducting the above credit items, amounted to \$4,834,900,000. Out of this sum Great Britain paid only about \$760,000,000 from its own resources and funded the balance of \$4,074,818,000 in the debt settlement with the United States.

### LOANS FOR COMMERCIAL, AS DISTINGUISHED FROM WAR PURPOSES

A more relevant issue than that concerning British expenditures is involved in the dispute as to what proportion of the British debt was expended for "commercial as distinguished from war purposes." Quite obviously there is no way of rigidly separating expenditures for "commercial" purposes from those for "war" purposes. In a war such as the last one the entire resources of the nations involved were used in the conflict and it is extremely difficult to distinguish between war and non-war expenditures. The National Industrial Conference Board has the following to say in regard to attempts to classify the wartime expenditures into such categories:

"Moreover on careful definition the distinctions to be drawn between war and non-war purposes seem to have little reality. It is extremely difficult to say what part of the loans might be regarded as having been expended for purposes unconnected with the war or unconnected with

the period of American participation in the war. The principal categories usually associated with this idea are: (1) pre-Armistice expenditures by the European Allied Governments in support of their civil populations or for protection of national trade interests; (2) expenditures to provide for commitments made prior to the entry of the United States in the war, such as interest and maturities; (3) all the post-Armistice cash advances, amounting to about \$2,000,000,000 (excluding the portion falling in category 2); (4) surplus war material sold abroad after the Armistice, amounting to about \$600,000,000."

#### **AMERICAN AND BRITISH INTERPRETATIONS**

If such a classification as that mentioned by the National Industrial Conference Board were followed and the statement of expenditures made by the American Treasury Department were accepted, the British loans for "commercial as distinguished from war purposes" would amount to a fairly high proportion of the present value of their debt to the United States. Among some of the items which would fall under the heading of "commercial purposes" are the following:

1. All loans to Great Britain which were made after the signing of the Armistice, amounting with interest to about \$660,000,000.
2. Interest and maturities on commercial loans contracted previous to American entrance into the war which amounts to about \$353,000,000.
3. Silver to India to the value of \$261,600,000 (a large part of this was advanced after the Armistice and would therefore be included under the first heading).
4. Advances to the British government for the maintenance of the exchange. Because this item is listed with cotton purchases it is impossible even to estimate the amounts borrowed for "pegging" operations.
5. Other pre-Armistice borrowings for the purpose of providing the civilian population with food and other supplies. It would be very difficult to estimate, quantitatively, the sums borrowed for these purposes.

It was apparently such a classification

of expenditures that Mr. Mellon had in mind when he made the statement in the Peabody letter that "It must be remembered that England borrowed a large proportion of its debt to us for purely commercial as distinguished from war purposes—to meet its commercial obligations maturing in America, to furnish India with silver, to buy food to be resold to its civilian population, and to maintain exchange."

The British have denied the possibility of making such a separation between war and non-war purposes. They point out that the war called forth the entire resources of their people, civil as well as military, and that the maintenance of the civilian population and the "pegging" of the exchange were quite as necessary for war purposes as keeping the army in the field. They also show that a large proportion of the British borrowing after the Armistice was for the purpose of buying American supplies for which contracts were made previous to the Armistice. Finally, they point out that the Liberty Loan Acts specifically limited American loans to the prosecution of the war.

#### **BRITAIN'S LOANS TO HER ALLIES**

The question has been raised in the recent controversy as to the proportion of the British debt accumulated in behalf of the Allies. It has been a common belief in England that a large part of the British debt was borrowed to re-loan to France and Italy, and that the United States insisted upon British guarantees before loaning money to the other nations. In the Balfour note of August 1, 1922 the British Secretary of State for Foreign Affairs gave expression to this idea by saying: "It should not be forgotten, though it sometimes is, that our liabilities were incurred for others, not for ourselves."

Mr. Philip Snowden, Chancellor of the Exchequer in the MacDonald cabinet has frequently made the same contention. In March, 1925 he said:

"These sums were borrowed by Great Britain either from her own citizens through the medium of war loans or from the United States. If it had not been neces-

sary for Great Britain to lend to her European allies to keep them going there would have been no need for us to borrow from America. The American debt was incurred by Great Britain to lend to France and Italy."

#### REASONS FOR BRITISH BORROWING IN U. S.

In spite of repeated assertions of this nature, there seems to be no evidence to support the contention that Great Britain incurred its indebtedness in behalf of the Allies. While it is true that the British Government acted as the purchasing agent in America for other governments, the sums borrowed for these purposes were returned to Great Britain with funds borrowed from the United States by the other Allies and placed to the credit of the British account. Mr. Albert Rathbone, who was in charge of foreign loans in the American Treasury department from 1918 to 1920, deals with the contention that Great Britain's indebtedness was incurred in behalf of the Allied governments as follows:

"The fundamental cause of Great Britain borrowing from us while loaning to the Allies was that there were commodities here which Great Britain required for her own use and was obliged to pay for in dollars which she borrowed from us, and there were commodities within the British Empire required by the Allies which had to be furnished them and for which they could not pay except from loans. The same condition existed, though to a smaller extent, in the case of France, which, while borrowing both of the United States and of Great Britain, nevertheless made loans to Belgium, to Italy, to Russia and to other of the Allies.

"The position of the British Government as both a borrower and lender unfortunately has led to some misapprehension regarding our own loans. In some quarters there has apparently existed the erroneous impression that while we made loans to other Allied governments we did so only on British security, or the equally mistaken view that the dollars Great Britain borrowed of us enabled her to make loans to other Allied Governments."

#### EVIDENCE OF SECRETARY MELLON

In a press release on August 24, 1922 Mr. Mellon answered inquiries on this point as follows:

"The statement that the United States Government virtually insisted upon a guarantee by the British Government of amounts advanced to the other Allies is evidently based upon a misapprehension. Instead of insisting upon a guarantee, or any transaction of that nature, the United States Government took the position that it would make advances to each government to cover the purchases made by that government and would not require any government to give obligations for advances made to cover the purchases of any other government. Thus, the advances made to the British Government, evidenced by its obligations, were made to cover its own purchases, and advances were made to the other Allies to cover their purchases."

In support of this statement Secretary Mellon quoted from a memorandum which the American Secretary of the Treasury handed to the British Ambassador in June, 1918. The Treasury memorandum reads as follows:

"So far as the purchases of the Allied Governments for war purposes within the United States and its territories and insular possessions are concerned it is the expectation of the Secretary of the Treasury to continue as heretofore the advances necessary to enable the financing of such approved purchases. The Secretary of the Treasury quite agrees with what he understands to be the views of the Chancellor of the Exchequer that advances shall be made to each Allied Government for the commodities purchased in the United States by or for it and that no Allied Government should be required to give its obligations for such purposes when merely serving as a conduit for the supply of the materials so purchased to another Allied Government. Any other course would indeed be incompatible with what the Secretary of the Treasury deems a cardinal principle which should be followed in respect to such advances, namely, that the Allied Government for the use of which the commodity is purchased must give its own obligation therefor and the obligation of any other Allied Government can not be accepted by the United States as an equivalent."

Mr. R. C. Leffingwell, who was Assistant Secretary of the Treasury in 1917, in an address on May 12, 1922 before the



American Academy of Political and Social Science in Philadelphia stated that "In one case only did Great Britain make advances after the United States entered the war for purchases by any of the Allies in the United States—that of Russia—and in that case only to the extent of contracts entered into by Russia and guaranteed by Great Britain before the United States entered the war. The amount is not important."

#### EXPLANATION OF THE LONDON ECONOMIST

The London *Economist* of January 10, 1925 in an editorial entitled "Inter-Allied Debt" replies to the Balfour contention as follows:

"Again, the fact that we are paying the United States is not in itself an argument for bringing pressure upon France, for it is not in any sense true, as is commonly supposed, that we borrow from the United States merely to re-lend to France and Italy. Our loans from America are quite independent of our loans to our European Allies. America lent to Italy, to France and to Great Britain monies required to enable them to make necessary purchases from the United States, and far the larger part of what we bought in America consisted of wheat, meat, metals, explosives, oil, fuel, and other essentials, either of our national existence or of our war effort. But France had to borrow not only in America; the fact that the greater part of her pig-iron production was in German hands and that her mines were destroyed, meant that she had to buy iron and steel and coal in Great Britain, as well as woolen cloth, chemicals and a great variety of manufactured products for which we advanced her sterling credits. It is an accident that the amount of these advances to France and Italy for purchases in Great Britain amounted during the latter part of the war to about the same amount as we had borrowed for British needs in the United States. But we cannot argue that if we had not been compelled to lend to our European Allies we need not have borrowed from America; the reason we had to borrow from the American Government was that—large though our internal loans might be—we had no means of securing credit in dollars. It is true we might have raised further sums by continuing to sell conscripted American securities, but it was already becoming difficult to make further sales, and this method of raising money would have been increasingly costly. On the other hand, the United States Government, as soon as it came into the war, was determined to control the purchases of ourselves and our Allies. For all parties concerned, therefore, it was the cheap-

est and most convenient plan for us to borrow from the United States Government. It is quite certain that even if France had not had to make any further purchases in Great Britain in 1917 and 1918, we should still have been under the necessity of borrowing in dollars in the United States in order to feed Great Britain and to provide the material which America alone could supply.

#### EXCHANGE REQUIREMENTS

In his reply to the American Treasury, Mr. Churchill asserted that "Great Britain provided sterling and neutral currencies to meet all her own requirements throughout the war, and in addition, bore the burden of covering the sterling requirements of her Continental allies. Had it not been for the fact that the United States did not feel able, upon entering the war, to relieve her of this additional burden, Great Britain would have been able to meet, from the resources she placed at the disposal of her allies, her expenditures in America and in all human probability the British debt to the United States would never have been incurred."

The implication of this contention is that Great Britain was compelled to assume the burden of financing her Allies, since the United States would not assume this increased financial burden.

Mr. Rathbone's evidence refutes this contention. His statement follows:

"After we entered the war, . . . Great Britain continued to furnish in the first instance most of the neutral finance required by France and Italy, but the United States Treasury, being prepared to bear its fair portion of the burden of securing finance for France and Italy in neutral countries, effected arrangements by which, after we entered the war, such purchases were ultimately in part financed by our dollar loans to France and Italy. The cost of the neutral finance so found after we entered the war was ultimately furnished, in the case of Italy, approximately one-half by the United States and one-half by Great Britain, and—in the case of France—something over one-half by the United States and the balance by Great Britain."

The explanation of these operations is given by Mr. Rathbone in the first part of the paragraph quoted above as follows:



"Various considerations had to be taken into account in determining how and to what extent the United States should aid in financing in neutral countries, necessary requirements of France and Italy, arising from the time we entered the war. Great Britain as the great creditor nation had available facilities for obtaining neutral finance which we, at that time a debtor nation, did not have. The apparent large balance of trade in favor of the United States, after there had been eliminated therefrom the United States exports paid for by the dollars which we had loaned to the Allied Governments, became a heavy adverse balance against the United States, and this seriously handicapped the ability of the United States to furnish financial aid to Allied Governments in neutral countries. Through its pre-war commercial interests and its well established war organizations, Great Britain was actually in a better position than we were in, or could put ourselves in, to handle the obtaining and utilizing of such neutral finance. Great Britain had capital interests in many neutral countries and for years the ocean transportation of exports and imports of neutral countries had been largely carried on by British ships. Between April 1917 and November 1918, as compared with the currencies of Sweden, Norway and Denmark, Holland, Switzerland, Spain, India, Japan, the Argentine, Chile, Peru and Bolivia, the dollar was at a discount, and the pound was at an even heavier discount than the dollar. Consequently, purchases in these countries, if paid for in dollars or in pounds at their current exchange value, meant costs largely in excess of the high war prices as measured in terms of the currencies of these countries. If we alone were to finance these neutral requirements, it was as a practical matter impossible

for us to delegate to Great Britain the control of the expenditure of our dollar loans for the neutral requirements of France and Italy for which they were unable themselves to provide. For the reasons elsewhere referred to, from the financial standpoint it was to our interest, and to the interest of Great Britain as well, that purchases which France and Italy could make in the United States or in Great Britain should be made there rather than in neutral countries."

#### AMERICAN "DISCRIMINATION AGAINST GREAT BRITAIN"

Because of the large proportion of the original debt that Great Britain is required to pay in relationship to the payments required of other countries many Englishmen are asking if they are not being unjustly discriminated against by the United States. This feeling is given expression in an editorial in the London *Daily Telegraph* for July 22, which asks: "Why this discrimination against Great Britain? Why discriminate adversely—and every time—against the one country which, of all America's large debtors, met her obligations punctually and to the very last penny?"

The amounts required under the debt-funding agreements with the principal allied countries and their present value considering the cost of money to the United States at  $4\frac{1}{4}$  per cent and 5 per cent is summarized in the following table:\*

	Great Britain	France	Italy	Belgium
Principal .....	\$ 4,600,000,000.00	\$4,025,000,000.00	\$2,042,000,000.00	\$417,780,000.00
Total to be Received ....	11,105,965,000.00	6,847,674,104.17	2,407,677,500.00	727,830,500.00
Present Value at $4\frac{1}{4}$ % .	3,788,470,000.00	1,996,509,000.00	528,192,000.00	225,000,000.00
Present Value at 5 % ...	3,296,948,000.00	1,681,369,000.00	426,287,000.00	191,766,000.00
Percentage ratio of present value to the principal, at $4\frac{1}{4}$ % .....	83%	48%	25%	54%

It will be seen that if the cost of money to the United States is assumed to be  $4\frac{1}{4}$  per cent the present value of the British settlement is 83 per cent of the principal—a percentage higher than that of any other country.

The position taken by the American debt-funding commission at the present time in reply to charges of discrimination is that the debt settlements are based upon the capacity of the debtor countries to pay. Great Britain is assumed to have a greater economic capacity than the other debtor na-

tions. The argument is also advanced that the proportion of the indebtedness for "purely commercial purposes" is larger than that of other countries. The actual proceedings of the U. S. Debt Funding Commission in their negotiations with other governments have been held in secret, so the only data available are the memoranda submitted by the debtor governments, and from these it is

\* $4\frac{1}{4}$  per cent is used as the cost of money to the United States because it approximates the average rate paid on Liberty bonds by the government. The rate that the money would bring at the present time has been used by some writers. This is generally assumed to be about 5 per cent.

not possible to discover concretely how the various agreements were reached. Likewise it is impossible to say why Italy was given terms so much more favorable than those given to France, or why such large payments were required of England, relative to the concessions made to other nations. The principle of capacity to pay is not a measuring rod that registers with unfailing accuracy.

#### **LEGAL LIMITATIONS ON AMERICAN LOANS**

The point has been raised by the Chancellor of the Exchequer that the American loans were limited by Congressional act to the specific purpose of the prosecution of the war. While it is true that the Liberty Bond Acts contained such limitations, it is a matter of common knowledge that the law was given a very liberal interpretation. After the signing of the Armistice Mr. Hoover made a special appeal to the President to continue to extend credit to the European governments. Mr. Hoover's appeal was based both upon humanitarian and selfish considerations. To have stopped abruptly the American advances to European nations would have cut off the demand for American goods and caused serious industrial depression in America. Because of these considerations American loans were advanced to Europe for two years after the Armistice.

#### **AMERICAN COMMITMENTS**

The claim has also been advanced that at the time the loans were made there were "understandings" that the obligations would later be cancelled. There is no evidence, however, of American commitments to any such policy. According to the Congressional Acts authorizing the European loans and the report of the committees to which the bills were referred in Congress it is very clear that the extension of credit to the Allied governments was purely in the nature of a loan. The borrowing governments were required to sign notes for each extension of credit. It is true that individual members of Congress in the debates on the bill expressed themselves as favorable to an outright gift to the Allies and there may also have been commitments

of such a nature by executive and diplomatic officials of the United States, but there is no evidence of official understandings to that effect.

#### **LARGER ASPECTS OF THE DEBT CONTROVERSY**

Although the recent dispute has been chiefly concerned with the more technical aspect of the debt funding relations between the United States and Great Britain, it has suggested many larger questions in regard to the whole debt funding policy of the United States in relationship to all the debtor countries. Because of Great Britain's position as both a borrower and lender in the last war the debt funding agreement between the United States and England was generally regarded as determining the policy that would be followed in the case of the other countries. This has been especially true because of Great Britain's policy which was announced in the "Balfour Note" of August 1, 1922 and repeated on several subsequent occasions. This was a communication sent to Great Britain's debtors by the British Secretary of State for Foreign Affairs in which the British policy was announced in the following words:

"But while His Majesty's Government are thus regretfully constrained to request the French Government to make arrangements for dealing to the best of their ability with Anglo-French loans, they desire to explain that the amount of interest and repayment for which they ask depends not so much upon what France and other Allies owe to Great Britain as on what Great Britain has to pay America. The policy favored by His Majesty is, as I have already observed, that of surrendering their share of German reparation, and writing off, through one great transaction, the whole body of inter-Allied indebtedness. But, if this be found impossible of accomplishment, we wish to make it understood that we do not in any event desire to make a profit out of any less satisfactory arrangement. In no circumstances do we propose to ask more from our debtors than is necessary to pay to our creditors."

A popular belief prevalent both in the United States and abroad is that the United States had demanded payment in full of the obligations of her debtors. This misconception has probably been due to the insistence on the part of administration leaders in Congress that the debt-funding agreements provided for the return to the

United States of the entire amount of the principal of the sums loaned by the United States to foreign countries. The only purpose of such statements is to mislead people into believing that the United States is collecting the full amount of its foreign loans. Obviously the payment only of the principal on a debt running for a period of sixty-two years is of little significance. The important consideration is the rate of interest paid during that time in relationship to the cost of the money to the creditor. If the United States could get  $4\frac{1}{4}$  per cent on its money, it is obviously losing on a debt settlement that pays only 1 per cent interest, and any settlement at terms lower than  $4\frac{1}{4}$  per cent is in effect a cancellation of the debt to the extent of the reduction of the interest rate. The statements in Secretary Mellon's recent letter to Mr. Peabody should serve to correct the erroneous impressions on this point. As a matter of fact, the various debt funding agreements provide for the cancellation of the following proportions of the debt to the United States in the case of the countries mentioned, if the cost of the money to the United States is figured at  $4\frac{1}{4}$  per cent.

Country	Proportion cancelled upon the basis of the present value of the debt with money at the cost of $4\frac{1}{4}$ per cent.
England .....	23%

France .....	52%
Belgium .....	46%
Italy .....	75%

#### FACTORS INVOLVED IN DEBT REVISION

There seems to be general agreement that if a revision of the debt settlements is undertaken in the future, both the capacity of the debtor nation to pay and the ability of the United States to receive payments will have to be taken into consideration. International financial transactions are not made by transporting actual currency or gold from one nation to another, but rather by an exchange of goods. The loans extended to the debtor nations by the United States were in the form of munitions, cereals and other commodities. Likewise repayment to the United States will be made in goods. That the United States will be able to receive such large amounts of foreign products as would have to be shipped to this country in order to pay the obligations of foreign governments and interest on the private American investments in other countries without serious injury to American business and industry, is extremely questionable. This is of especial importance in view of the American tariff policy which is designed to keep foreign goods from entering the United States.

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